

August 14, 2003

Luly Massaro, Clerk
Public Utilities Commission
89 Jefferson Blvd.
Warwick, RI 02888

Re: Docket No. 3497

Dear Ms. Massaro,

The Public Utilities Commission ("Commission") has requested the Division of Public Utilities and Carriers ("Division") to provide the Commission with its opinion regarding the following legal issue: Does the Commission possess the legal authority to design rates so as to enable recovery of a tangible property tax increase imposed by the Town of Cumberland from utility customers located only in the Town of Cumberland?

Fees, rates and charges for drinking water are determined by a host of different factors including the difference in costs based upon different points of delivery and the recovery of all fixed and variable operating costs. G.L. § 46-15.4-6. The Rhode Island Supreme Court, further, has held that the Commission possesses the right to allocate the cost of service among customer classes. Violet v. Narragansett Electric Co., 505 A.2d 1149, 1151 (R.I. 1986). Factors, other than cost (such as the value of service to the community, the adequacy of service, past discrimination, the public benefit, and environmental considerations), may warrant a modification of rates dictated by the cost-of-service methodology. United States v. Public Utilities Comm'n, 635 A.2d 1135, 1141 (R.I. 1993); Town of Narragansett v. Malachowski, 621 A.2d 190, 196 (R.I. 1993); United States v. Public Utilities Comm'n, 393 A.2d 1092, 1097 (R.I. 1978).

In other jurisdictions, it has been held that a municipal water utility may charge more for water service delivered outside its corporate limits than for the same service delivered to users within the corporate limits. Village of Fox Point v. Public Serv. Comm'n, 7 N.W.2d 571 (Wisc. 1943); Collier v. Atlanta, 173 S.E. 853 (Ga. 1934); Durant v. Beverly Hills, 102 P.2d 759 (Dist Ct. App. Cal. 1940); Frazer v. City of Pueblo, Case 1384, Decision No. 6459 (Col. PUC 1935). This principle particularly holds true in order to pay for the cost of extending service outside the municipal corporate limits, Borough of Ambridge v. Pennsylvania Public Utility Comm'n, 8 A.2d 429 (Pa. Super. Ct. 1939), or to pay for increased operational costs outside the city's limits. Village of

Fox Point v. Public Service Comm'n, 7 N.W.2d 571 (Wisc. 1943). These cases have been upheld more recently in Hansen v. City of San Buena Venture, 729 P.2d 186 (Cal. 1987) and Zepp v. Mayor & Council of the City of Athens, 339 S.E.2d 576 (Ga. 1986).

In light of the weight of this precedent, the Division believes that the Commission does possess the legal authority to approve a rate design that enables the PWSB to recover an increase in tangible property taxes only from Cumberland ratepayers. Generally, however, the Commission has been reluctant to exercise its legal authority in this regard to its utmost limits. The Division's expert consultant, Thomas S. Catlin, explains:

Property subject to taxation is normally used for the benefit of all customers. Under such circumstances, it would be inappropriate to recover the property taxes assessed by a given municipality only from the customers located in that municipality. Instead, it is normally appropriate that all property taxes be recovered from all customers as part of base rates.

T. Catlin, Direct Testimony, Page 6.

In the present case, the Town of Cumberland has not provided the Division with the information and documentation necessary to determine which "assets the taxes on tangible property are associated with," the "bases for the large increase in valuation and taxes," whether "those taxes are associated with property which benefits all customers," or whether the taxes "are comparable to taxes assessed by other jurisdictions." T. Catlin, Direct Testimony, Page 6. Under the unique circumstances of this case, then, the Commission may wish to make an exception to the general rule and allow recovery of the increase in taxes on tangible property directly from customers in the Town of Cumberland. Compare In Re: Interstate Navigation Co., Docket 2484, Order 15378 (1997).

Respectfully Submitted,

Division of Public Utilities and Carriers,
By its attorneys,

Leo J. Wold, # 3613
Special Assistant Attorney General

cc: Service List